UNITED STATES DISTRICT COURT
SOUTHERN DISTRICT OF NEW YORK

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LUDLOW ESSEX PARTNERS LLC, NATHAN HALEGUA and MARTIN D. NEWMAN, Plaintiffs, - against - WELLS FARGO BANK, N.A., Defendant.	Case No. 1:17-cv-02042
--X	

PLAINTIFFS' MEMORANDUM OF LAW
IN OPPOSITION TO DEFENDANT'S MOTION TO DISMISS

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Plaintiffs, Ludlow Essex Partners LLC ("Ludlow"), Nathan Halegua ("Halegua") and Martin D. Newman ("Newman") (collectively the "Plaintiffs"), submit this Memorandum of Law in opposition to the motion of Wells Fargo Bank, N.A. ("Defendant" or "Wells Fargo") to dismiss Plaintiffs' Complaint (the "Complaint") pursuant to Federal Rule of Civil Procedure 12(b)(6).

INTRODUCTION

This action was born of a theft, but it is not an action solely about a theft. It is equally an action about the total lack of preventive measures employed by Wells Fargo to not be a tool for fraudsters and protect moneys that pass through its accounts. Plaintiffs are not asking that Wells Fargo police all transactions that are conducted through the bank; Plaintiffs do seek to hold Wells Faro accountable for its utter disregard of protocols intended to discourage or prevent use of the bank as a receptacle of illegally procured money. It is not disputed that Plaintiffs' money was stolen through the use of a fraudulently opened and maintained bank account at Wells Fargo. Although the crime was committed by a Wells Fargo customer, an integral element of the theft was the negligence of Wells Fargo in opening and maintaining the account and turning a blind eye to the dubious nature of the customer. For example, did Wells Fargo require and maintain information about the principals of the purported corporate entity? Were there corporate resolutions? Were there articles of incorporation requested and obtained? The negligent or willful nonfeasance permitted the criminals to use the bank as an instrument in their criminal scheme. The ease these thieves enjoyed in operating unfettered is directly attributable to Wells Fargo. This matters because Plaintiffs would not have been damaged but for Wells Fargo's actions.

In bringing this motion to dismiss, Defendant has cast itself in the role of an unwitting and innocent depository. Such characterization is undeserved. In fact, Wells Fargo is grossly miscast in that role. The truth of the matter is that Defendant has recently been exposed for engaging in a pattern of reckless conduct whereby numerous bank accounts were irresponsibly or even furtively opened and allowed to exist all for collection of fees. This pattern of opening accounts may have started due to the greed of Wells Fargo's employees who sought to generate fees and commissions to which they were not entitled, but the ability of Wells Fargo employees to do so was made possible specifically because Wells Fargo engaged in a complete abandonment of the safeguards that are universally accepted in the banking industry.

It is far too simple for Wells Fargo to assert that it has no duty of care to Plaintiffs and that the case should be dismissed on that ground. In actuality, the caselaw that Defendant has cited does not establish as sweeping a proposition as Defendant asserts. Although it may be the case that a bank cannot be held liable for the criminal acts of others, that does not mean that a bank cannot be held liable for its own willfully negligent and myopic conduct which directly leads to financial damages like those suffered by Plaintiffs. For the reasons set forth below, Defendant's motion should be denied and Plaintiffs should be afforded their day in court.

WELLS FARGO WAS ON NOTICE OF THE USE OF BANKS AS INSTRUMENTS OF FRAUD AND DISREGARDED THE DANGER

In August 2001, the agencies of the Federal Financial Institutions Examination Council ("FFIEC") (which included the Board of Governors of the Federal Reserve System, Federal Deposit Insurance Corporation, National Credit Union Administration, Office of the Comptroller of Currency, and the Office of Theft Supervision) issued guidelines entitled "Authentication in an Internet Banking Environment" which "focused on risk management controls necessary to authenticate the identity of retail and commercial customers accessing internet-based financial services." The guidelines urged "[f]inancial institutions offering internet-based products and services to their customers [to] use effective methods to authenticate the identity of customers using these products and services" with the authentication techniques "appropriate to the risks associated with those products and services." The guidelines warned that "single-factor authentication, as the only control mechanism, [was] inadequate in the case of high-risk transactions involving access to customer information or the movement of funds to other parties."

In October 2005, the FFIEC agencies issued a supplement to the guidelines, warming of the "increasingly hostile online environment," and recommending that institutions "perform periodic risk assessments [at least once every twelve months] and adjust their control mechanisms as appropriate in response to changing internal and external threats." The agencies reported heightened "expectations regarding customer authentication, beyond security, or other controls in the increasingly hostile online environment." The agencies defined "high-risk transactions" as "electronic transactions involving access to customer information or the movement of funds to other parties," and concluded that "financial institutions should implement more robust controls as the risk level of the transaction increases."

By December 2015, Wells Fargo was aware of, or should have been aware of increasingly occurring scams and thefts using wire transfers and fraudulent accounts for the transfer of stolen funds. By that time, Wells Fargo was aware of, or should have been aware of the need for appropriate and effective identification of and authentication of its customers and the need to ensure that its accounts were not used as an instrument of fraud and illegality.

Upon information and belief, Wells Fargo incentivized its employees to open new accounts without taking proper precautions to make certain that these accounts belonged to *bona fide* individuals or businesses. This resulted in approximately two million bogus Wells Fargo accounts being established without customers' permission or authentication. In short, Wells Fargo created an aggressive sales culture in which its employees ignored internal procedures and other banking safeguards. Further, Wells Fargo did not undertake appropriate protocols to vet and authenticate new customer accounts.

As a result of Wells Fargo's actions, Wells Fargo recently was forced to fire 5,300 employees in connection with creating millions of fake Wells Fargo accounts. Relatedly, Wells Fargo's Chief Executive Officer, John Strumpf, was forced to retire suddenly in October 2016, in the process forfeiting nearly $41,000,000 in stock awards, in connection with the uncovering of Wells Fargo's practice of allowing millions of fake bank accounts to be created and maintained. Further, Wells Fargo has been hit with $185,000,000.00 is federal and state fines and paid $110,000,000.00 to settle a class-action lawsuit related to these breaches.

STATEMENT OF FACTS AND PROCEDURAL HISTORY

David Levy ("Levy") together with plaintiffs, Nathan Halegua ("Halegua") and Martin Neman ("Newman") are members of plaintiff, Ludlow Essex Partners LLC ("Ludlow Essex").

In or about November 2015, Ludlow Essex decided to make distributions to its members. In connection with the aforementioned distributions, Ludlow Essex resolved to make a distribution of $250,000.00 to Levy (the "Distribution").

Levy controls an email account known as EASTSIDE10021@aol.com. By email dated December 1, 2015 at 9:46 A.M., which was sent from EASTSIDE10021@aol.com, Ludlow Essex's controller was instructed to make the Distribution to Levy by wire transfer to a bank account maintained by Signature Bank.

A second email from EASTSIDE10021@aol.com was sent 16 minutes later (the "Fraudulent Email") to Ludlow Essex's controller stating that the earlier referenced Signature bank account could not accept wires at the time due to an audit and instructed Ludlow Essex to make the Distribution by wire transfer to a bank account maintained by Wells Fargo with the named beneficiary of "JGM Global Ventures Inc." (the "Fraudulent Account"). Levy did not send the Fraudulent Email, and it is believed that individuals associated with JGM Global Ventures Inc. did.

JGM Global Ventures Inc. was incorporated in New York on November 13, 2015. Upon information and belief, JGM Global Ventures, Inc. opened an account with Wells Fargo shortly after incorporation (the "Fraudulent Account"). It is further believed that Wells Fargo did not investigate or undertake any vetting of JGM Global Ventures Inc. prior to allowing it to open the Fraudulent Account. Wells Fargo knew or should have known that JGM Global Ventures Inc. was not a *bona fide* corporation.

On December 14, 2015, Ludlow Essex wired the Distribution to Wells Fargo via the Fraudulent Account. Levy did not receive the Distribution.

After learning that Levy did not receive the Distribution, Halegua spoke with a Wells Fargo employee who confirmed that Wells Fargo received the Distribution and that the Distribution was paid to the Fraudulent Account. The Wells Fargo employee further stated that $159,247.55 of the Distribution had been withdrawn from the Fraudulent Account by an unknown person on December 16, 2015. At that time, $90,752.45 of the Distribution remained in the custody of Wells Fargo in the Fraudulent Account.

Wells Fargo returned $90,752.45 of the Distribution to Ludlow Essex. Ludlow Essex then paid Levy the returned $90,752.45 from the Distribution. Halegua and Newman have since personally paid Levy the $159,247.55 that was stolen from the Distribution.

Ludlow Essex's affiliated company, Citi-Urban Management Corp. ("Citi-Urban") maintains a policy of insurance with Westchester Fire Insurance, Co. (the "Policy"). Ludlow Essex and Citi-Urban filed an insurance claim under the Policy (the "Claim") associated with the theft of the Distribution. Westchester Fire Insurance, Co. paid $75,000 on the Claim. After fees and expense, Ludlow Essex received a net payment of $52,500 on the Claim from Westchester Fire Insurance, Co.

Accordingly, $106,747.55 of the Distribution remains unaccounted for. Plaintiffs have brought the instant action seeking damages against Wells Fargo as a result.

Plaintiffs commenced this action in New York State Supreme Court ("State Court") on February 22, 2017. *See* Clarke Decl. at Exhibit "1". Wells Fargo's time to respond to Plaintiffs' complaint was extended through April 3, 2017 per stipulation filed in State Court on March 14, 2017. *See* Clarke Decl. at Exhibit "2". Defendant filed the instant motion to dismiss on April 4, 2017, one day after its response to the Complaint was due.

STANDARD OF REVIEW UNDER RULE 12(b)(6)

Federal Rule of Civil Procedure 8(a)(2) requires only "a short and plain statement of the claim showing that the pleader is entitled to relief." Specific facts are not necessary; the statement need only "'give the defendant fair notice of what the ... claim is and the grounds upon which it rests.'" *Bell Atlantic Corp. v. Twombly,* 550 U.S. 544, 555, 127 S.Ct. 1955, 167 L.Ed.2d 929 (2007) (quoting *Conley v. Gibson,* 355 U.S. 41, 47, 78 S.Ct. 99, 2 L.Ed.2d 80 (1957)).

When deciding a motion to dismiss under Rule 12(b)(6), the Court must accept as true all well-pleaded factual allegations of the complaint and draw all inferences in favor of the pleader. *See City of Los Angeles v. Preferred Communications, Inc.,* 476 U.S. 488, 493, 106 S.Ct. 2034, 90 L.Ed.2d 480 (1986); *Miree v. DeKalb County,* 433 U.S. 25, 27 n. 2, 97 S.Ct. 2490, 53 L.Ed.2d 557 (1977) (referring to "well-pleaded allegations"); *Mills v. Polar Molecular Corp.,* 12 F.3d 1170, 1174 (2d Cir.1993). In other words, it is necessary for the Court to view the complaint in the light most favorable to the plaintiff. *See Scheuer v. Rhodes,* 416 U.S. 232, 237 (1974); *Yoder v. Orthomolecular Nutrition Inst., Inc.,* 751 F.2d 555, 562 (2d Cir.1985).

Dismissal is proper only when "it appears beyond doubt that the plaintiff can prove no set of facts in support of his claim which would entitle him to relief." *Conley v. Gibson,* 355 U.S. 41, 45–46, 78 S.Ct. 99, 2 L.Ed.2d 80 (1957); accord *Cohen v. Koenig,* 25 F.3d 1168, 1172 (2d Cir.1994).

ARGUMENT

Defendant's motion is premised on the overbroad assertion that a bank is completely insulated from civil liability under theories of common law negligence and the New York General Business Law if a plaintiff is a non-customer. Such a sweeping position is not supported under controlling law nor when applied to the facts of this case. Plaintiffs have plead sufficient facts to warrant the case to continue. Accordingly, Defendant's motion should be denied, Wells Fargo should file an answer and the parties should be directed to conduct discovery.

1. **Plaintiffs Have Stated A Claim for Negligence**

To establish a prima facie case of negligence under New York law, "a plaintiff must demonstrate (1) a duty owed by the defendant to the plaintiff, (2) a breach thereof, and (3) injury proximately resulting therefrom." *Lerner v. Fleet Bank, N.A.,* 459 F.3d 273, 286 (2d Cir. 2006) (citing *Solomon ex rel. Solomon v. City of New York,* 66 N.Y.2d 1026, 1027, 489 N.E.2d 1294, 1294, 499 N.Y.S.2d 392, 392 (1985)0; *see also King v. Crossland Sav. Bank,* 111 F.3d 251, 259 (2d Cir.1997).

In support of its motion to dismiss, Defendant argues that it is immune from liability for its negligence based on the proposition that "[b]anks do not owe non-customers a duty to protect them from the intentional torts of their customers." *See* Def. Mem. at p. 4 (citing *Lerner v. Fleet Bank, N.A.*, 459 F.3d 273, 286 (2d Cir. 2006)).

Defendant overstates the rule in *Lerner*. There is no absolute bar on finding a bank liable to a non-customer for negligence. The narrow ruling in *Lerner* is that "a depositary bank has no [general] duty to monitor fiduciary accounts maintained at its branches in order to safeguard funds in those accounts from fiduciary misappropriation." *Lerner,* 459 F.3d at 287 (quoting *Norwest Mortgage, Inc. v. Dime Sav. Bank of N.Y.,* 280 A.D.2d 653, 654, 721 N.Y.S.2d 94 (N.Y.App.Div.2001)). *Lener* went on to add that there is a duty to make reasonable inquiry and endeavor to prevent a diversion where a depository bank has "notice or knowledge that a diversion is intended or being executed." *Id.* (quoting *In re Knox,* 64 N.Y.2d 434, 438, 488 N.Y.S.2d 146, 477 N.E.2d 448 (1985)). Thus, the inquiry becomes whether Defendant had notice or knowledge that its customer was opening an account for legitimate purposes. Stated otherwise, did Wells Fargo heed and adhere to cautions given by the FFIEC when they warned the banking industry of the illegitimate and illegal use of bank accounts in fraudulent schemes. If, as Plaintiffs allege, Wells Fargo did not, then Wells Fargo should be held to account for the damages resulting from such willful ignorance or disregard. This is necessarily a fact-specific inquiry, ill-suited to summary disposition, much less by a pre-answer motion to dismiss.

Defendant's reliance on this Court's decision in *Tzaras v. Evergreen Int'l Spot Trading, Inc.* 2003 WL 470611 (S.D.N.Y. 2003) is likewise misplaced. In *Tzaras*, this Court found it appropriate to grant the defendant bank's motion to dismiss plaintiff's negligence claim on the ground that it owed no duty to prevent fraud. *Id.* at *6. However, that comparison relies on a mischaracterization of Plaintiffs' claims. Whereas the defendant bank in *Tzaras* was sued for failing to protect a non-customer plaintiff, Plaintiffs have not brought this case on the ground that Wells Fargo failed to protect Plaintiffs from fraud and theft (although Wells Fargo did so fail) but rather that Wells Fargo engaged in banking practices, namely the opening of bank accounts without proper checks, that allowed thieves a safe haven from which it could conduct crimes. In other words, it is not disputed that banks generally do not owe non-customers a duty of care to protect from third-party acts, but that does not mean that a bank can neglect all of the warning signs about financial fraud and shirk its own internal procedures to allow fraudulent accounts to be established. Wells Fargo doing so proximately caused Plaintiffs' damages.

Based on the foregoing, Defendant's motion should be denied.

2. **Plaintiffs Have Stated A Claim for Violation of New York General Business Law §349**

New York General Business Law Section 349 " 'was designed to protect consumers from various forms of consumer fraud and deception.' " *Twentieth Century Fox Film Corp. v. Marvel Enterprises, Inc.,* 155 F.Supp.2d 1, 25 (S.D.N.Y.2001) (quoting *Smith v. Triad Mfg. Group, Inc.,* 255 A.D.2d 962, 681 N.Y.S.2d 710, 712 (4th Dep't 1998)). Section 349 "declares unlawful 'deceptive acts or practices in the conduct of any business, trade or commerce or in the furnishing of any service.' " *Riordan v. Nationwide Mut. Fire Ins. Co.,* 977 F.2d 47, 51 (2d Cir.1992) (internal brackets omitted) (*quoting* General Business Law § 349(a)); *accord Highlands Ins. Co. v. PRG Brokerage, Inc.,* No. 01 Civ. 2272(GBD), 2004 WL 35439, at *9 (S.D.N.Y. Jan. 6, 2004); *Kforce, Inc. v. Alden Personnel, Inc.,* 288 F.Supp.2d 513, 518 (S.D.N.Y.2003). The statute provides a private right of action to any person injured by a business' deceptive act or practice. *Riordan,* 977 F.2d at 51 (citing General Business Law § 349(h)); *accord Am. Med. Ass'n v. United Healthcare Corp.,* No. 00 Civ. 2800(LMM)(GWG), 2003 WL 22004877, at *6 (S.D.N.Y. Aug. 22, 2003); *Gucci Am., Inc. v. Duty Free Apparel, Ltd.,* 277 F.Supp.2d 269, 272 (S.D.N.Y.2003).

"A plaintiff under section 349 must prove three elements: first, that the challenged act or practice was consumer-oriented; second, that it was misleading in a material way; and third, that the plaintiff suffered injury as a result of the deceptive act." *Stutman v. Chem. Bank,* 95 N.Y.2d 24, 29, 709 N.Y.S.2d 892, 731 N.E.2d 608 (2000) (citations omitted); *accord Maurizio v. Goldsmith,* 230 F.3d 518, 521–22 (2d Cir.2000); *Lava Trading Inc. v. Hartford Fire Ins. Co.,* No. 03 Civ. 7037(PKC), 2004 WL 555723, at *3 (S.D.N.Y. March 19, 2004); *Smith v. Chase Manhattan Bank, USA, N.A.,* 293 A.D.2d 598, 741 N.Y.S.2d 100, 102 (2d Dep't 2002). "In addition, a plaintiff must prove 'actual' injury to recover under the statute, though not necessarily pecuniary harm." *Stutman,* 95 N.Y.2d at 29, 709 N.Y.S.2d 892, 731 N.E.2d 608.

It is well established that omissions may provide the basis for such claims. *See Oswego Laborers' Local 214 Pension Fund v. Marine Midland Bank, N.A.,* 85 N.Y.2d 20, 26 (1995) ("objective definition of deceptive acts and practices" includes "misrepresentations or omissions"); *see also Stutman,*95 N.Y.2d at 29; *Solomon,* 9 A.D.3d at 52. Deceptive practices, however, "need not reach the level of common law fraud to be actionable under [S]ection 349." *Boule,* 328 F.3d at 94 (quoting *Stutman,* 95 N.Y.2d at 29).

Thus, as the New York Court of Appeals has stated, "a *prima facie* case [for a Section 349 claim] requires a showing that defendant is engaging in an act or practice that is deceptive or misleading in a material way and that plaintiff has been injured by reason thereof." *Oswego*

Laborers' Local 214 Pension Fund v. Marine Midland Bank, N.A., 85 N.Y.2d 20, 24, 647 N.E.2d 741, 744 (1995).

The statute does not require proof of justifiable reliance. *Id.* at 744. Accordingly, §349 claims are not subject to the heightened pleading requirements of Federal Rule of Civil Procedure 9(b). *See Braynina v. TJX Companies, Inc.*, No. 15 CIV. 5897 (KPF), 2016 WL 5374134, at *4 (S.D.N.Y. Sept. 26, 2016).

Plaintiffs have set forth a legally sufficient claim under Section 349 under the *Stutman* test which has been adopted by this court. *See Bildenstein v. MasterCard Intern., Inc.*, 329 F.Supp.2d 410 (S.D.N.Y. 2004). As set forth in the Complaint, it is believed that Wells Fargo incentivized its employees to open new accounts without taking proper precautions to make certain that these accounts belonged to *bona fide* individuals or businesses. (Complaint, ¶31).

It is beyond dispute that Wells Fargo opening and maintaining bogus bank accounts is consumer oriented activity as Defendant is a national banking association. Similarly, Wells Fargo's omissions in failing to inform its customers that it was in fact an unregulated haven for thieves and scoundrels to conduct their business with a veneer of legitimacy. Claims under Section 349 are viable "where the business alone possesses material information that is relevant to the consumer and fails to provide this information." *Oswego,* 85 N.Y.2d at 26. Finally, it can hardly be disputed that Plaintiffs have clearly been injured as a result of Wells Fargo's willfully ignorant environment which facilitated fraudsters' unfettered use of the bank as an instrument of their scam.

Defendant bases its motion to dismiss Plaintiffs' General Business Law §349 claim again largely on the fact that Plaintiffs are not Wells Fargo customers, arguing that Plaintiffs are required to show that Wells Fargo's actions denied Plaintiffs knowledge of a fact that would have affected their choice of bank. Def. Mem. at 7. Defendant's argument ignores the Court's ruling in the second *Bildstein* litigation, which rejected such a sweeping proposition. *See Bildstein v. MasterCard Int'l, Inc.,* No. 03 CIV.9826I(WHP), 2005 WL 1324972 (S.D.N.Y. June 6, 2005) ("*Bildstein II*").

As stated in *Bildstein II,* privity is not required to state a Section 349 claim. Id. at *3. *See also, In re Tertiary Butyl Ether Prods. Liab. Litig.,* 175 F.Supp.2d 593, 630-31 (S.D.N.Y.2001) ("Indeed, there is no requirement of privity, and the victims of indirect injuries are permitted to sue under [Section 349].") (internal quotation marks and citation omitted). As such, Defendant's simple assertion that Plaintiffs are not Wells Fargo customers is not a basis to dismiss.

For the reasons set forth above, Plaintiffs have pleaded a cause of action under Section 349 of the General Business Law. Defendant's motion should be denied and the parties directed to proceed with discovery.

3. **Defendant's Motion Should be Denied as Untimely**

Plaintiffs commenced this action in New York State Supreme Court ("State Court") on February 22, 2017. Wells Fargo's time to respond to Plaintiffs' complaint was extended through April 3, 2017 per stipulation filed in State Court on March 14, 2017. Defendant filed a notice of removal of this action to this Court in State Court on March 21, 2017. Defendant filed the instant motion to dismiss on April 4, 2017, one day after its response to the Complaint was due.

Based on the foregoing, Defendant's motion should be denied as untimely.

4. **Leave to Amend Should be Granted if Deemed Necessary**

To the extent the Court feels that there are any infirmities with the Complaint, it is respectfully submitted that the proper remedy is not dismissal but instead to afford Plaintiffs an opportunity to replead and to serve an Amended Complaint.

Where a complaint is dismissed for failing to state a claim upon which relief can be granted under Rule 12(b)(6), it is "the usual practice" to allow leave to replead. *Cortec Indus.*, 949 F.2d 42, 48 (2d Cir. 1991); *see also Ronzani v. Sanofi* S.A., 899 F.2d 195, 198 (2d Cir.1990); *Devaney v. Chester,* 813 F.2d 566, 569 (2d Cir. 1987). Indeed, if a plaintiff has at least colorable grounds for relief, justice requires leave to amend complaint following dismissal for failure to state claim. *Old Republic Ins. Co. v. Hansa World Cargo Service, Inc.* 170 F.R.D. 361, 370 (S.D.N.Y. 1997).

Plaintiffs should be afforded an opportunity to amend their Complaint in the event the Court finds it lacking.

CONCLUSION

Plaintiffs have stated claims for negligence and violations of New York's General Business Law §349. Accordingly, Defendant's motion should be denied in its entirety.

Dated: New York, New York
May 9, 2017

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UNITED STATES DISTRICT COURT
SOUTHERN DISTRICT OF NEW YORK

LUDLOW ESSEX PARTNERS LLC, NATHAN HALEGUA and MARTIN D. NEWMAN, Plaintiffs, - against - WELLS FARGO BANK, N.A., Defendant.	:	Case No. 1:17-cv-02042

CERTIFICATE OF SERVICE

I HEREBY CERTIFY that on May 9, 2017, a true and correct copy of the foregoing Memorandum of Law was filed electronically with the Clerk of the Court using the CM/ECF system, which will send notification of such filing to all counsel of record.

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